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TO RUEHC/SECSTATE WASHDC 7062
INFO RHEFDIA/DIA WASHINGTON DC
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RHEFHOT/HOTR WASHINGTON DC//USDAO ISLAMABAD PK//
RUWSMXI/AMC INTEL CEN SCOTT AFB IL//INO/J2-J//
RUEPVAA/CDR JSOC FT BRAGG NC//J2/HSE//
RHMFISS/CDR USCENTCOM MACDILL AFB FL//CCJ2-JCH/HSE//
RHLFABN/CDR USESUCOM ABNCP VAIHINGEN GE//ECJ2/ECJ3/ECJ5-A//
RHMFISS/CDR USSOCOM MACDILL AFB FL//SOJ2/HSE//
RHMFIUU/CDR USTRANSCOM TCJ2 SCOTT AFB IL
RHMFISS/CDRUSAREUR HEIDELBERG GE//AEAGB-IAD//
RUEAIIA/CIA WASHINGTON DC//DDI/OEA//
RUEPVAA/COMJSOC FT BRAGG NC
RHMFIUU/COMSOCCENT MACDILL AFB FL//SOCJ2/HSE//
RHEFDIA/DIA WASHINGTON DC//DHO-3//
RHEFDIA/DIA WASHINGTON DC//MIO-4//
RUETIAA/DIRNSA FT GEORGE G MEADE MD//M112/S2132HT//
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RUEKJCS/JOINT STAFF WASHINGTON DC//J2/J5-EUR//
RUZFNAI/NASIC WRIGHT PATTERSON AFB OH
RUZFNAI/NASIC WRIGHT PATTERSON AFB OH//DEKA/FCTP//
RUZFNAI/NASIC WRIGHT PATTERSON AFB OH//DXOA/TAAO//
RHEFNGB/NGIC INTEL OPS CHARLOTTESVILLE VA
RHEFNGB/NGIC INTEL OPS CHARLOTTESVILLE VA//IANG-CE-CM/IANG-GS-AA//
RHEFNGB/NGIC INTEL OPS CHARLOTTESVILLE VA//IANG/CE/CECM//
RUCXONI/ONI WASHINGTON DC//32/211//
RUEALGX/SAF WASHINGTON DC
RUEKJCS/SECDEF WASHINGTON DC//USDP-ISA-ADMIN//
RULWAAM/STRATCOM IDHS-90 OFFUTT AFB NE//J22123//
RUEPGAA/US SURVEY DIV SHAPE BE
RUMICEA/USCENTCOM INTEL CEN MACDILL AFB FL
RUEHIL/USDAO ISLAMABAD PK
RUCQSAB/USSOCOM INTEL MACDILL AFB FL
RUEHLO/AMEMBASSY LONDON 2260
RUEHNE/AMEMBASSY NEW DELHI 6024
RUEHBUL/AMEMBASSY KABUL 1417
RUEHLH/AMCONSUL LAHORE 8423
RUEHKP/AMCONSUL KARACHI 2823
RUEHPW/AMCONSUL PESHAWAR 7483
RUEHRC/DEPT OF AGRICULTURE WASHDC
RUEATRS/DEPT OF TREASURY WASHDC
RUCPDOG/DEPT OF COMMERCE WASHDC
RHEBAAA/DEPT OF ENERGY WASHDC

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SENSITIVE
SIPDIS

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SUBJ: BI-WEEKLY REPORT ON ECONOMIC ISSUES, January 20, 2010

TOP STORIES

1. (SBU) State Bank of Pakistan (SBP) releases FY10 midterm report. Business Recorder reported on January 13 that the SBP's overall picture of the economy was relatively optimistic with most key indicators continuing the positive trends that began at the end of last quarter. According to SBP projections, GDP growth is likely to reach 3.3 percent, and exports should total \$18.5 to \$19 billion in FY10. The fiscal deficit is expected to be comparable to last year's, remaining between 4.7 - 5.2 percent of GDP, whereas the current account deficit is likely to fall to 3.7 - 4.7 percent of GDP from FY 09's 5.3 percent. The SBP anticipates that the GOP will face major challenges in improving the tax-to-GDP ratio, which currently stands at 9.8 percent. (Comment: In light of the weak foreign direct investment and marginal growth in industrial

production the SBP's GDP projection may be ambitious. End Comment)

12. (SBU) Asian Development Bank (ADB) audit reveals irregularities in Rental Power Plants (RPPs) awards. Business Recorder reported on January 18 that the ADB found inconsistencies in the criteria used to award the RPP contracts. The report emphasized that, in some cases, the RPP agreements were awarded to well-connected individuals rather than to the best qualified project. Implementation of the RPPs was also noted with concern, as the GOP would need to increase electricity prices 25 to 45 percent to fund more expensive rental power. (Comment: The draft ADB report completed in December is now making its way through the various GOP ministries. The report lays out a series of scenarios for the GOP on the cost/benefit of introducing RPPs, with an emphasis on the benefits of moving forward with fewer RPPs (most likely 8) than the 14 RPPs currently approved. End Comment)

13. (SBU) Prime Minister replaces the Minister of Health and sacks the drug controller. The News reported on January 16 that the Prime Minister's actions came in response to allegations of widespread nepotism and corruption within the Ministry of Health (MOH). According to the article, MOH officials were hiring under-qualified, politically-connected individuals to run multi-million dollar national health programs such as the National Maternal and Child Health program. The report indicated that there were also spillovers into the drug registration process, claiming that certain pharmaceutical companies were bribing top level MOH officials to

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fast track the registration of their new drugs, a process which typically takes several months and, in some cases, years to complete. (Comment: Contacts from the pharma industry have often complained about the MOH's inefficiencies. Whether or not this change in leadership will help to clear some of the bottlenecks and the bureaucratic red tape within the ministry remains to be seen. End Comment)

14. (SBU) The Sui Northern Gas Pipelines Limited (SNGPL) suspends provision of gas to textile mills. On January 12, The News reported that SNGPL had indefinitely cut the supply of gas to all textile mills located in Punjab and NWFP. Representatives from the Punjab chapter of the All Pakistan Textile Mills Association complained that these actions were contrary to the Cabinet Committee on Gas Load Management's decision to only suspend gas two days a week. They added that local textile industries would have no backup energy sources left to run their operations as they were already dealing with 10 to 12 hour blackouts per day. (Comment: Due to the spikes in domestic consumption during the winter months, textile and other industries receive nine-month contracts for gas and are expected to find other fuel sources for the remaining 3 months. However, this drama plays out annually, with gas users crying foul when the GOP makes unrealistic promises to supply gas over and above the agreed nine months.)

TEXTILES

15. (SBU) The textile industry bitterly divided over a new limit on cotton yarn exports. On January 10 Business Recorder reported that the Cabinet Committee on Textiles is imposing a cap of 50,000 kilograms per month on yarn exports. This is approximately 20 percent below current export volumes. Feeling that the limit was too generous and would leave Pakistani manufacturers short of raw materials, the Pakistan Cotton Fashion Apparel Manufacturers and Exporters Association threatened to go on strike. Conversely, the All Pakistan Textile Mills Association was deeply critical of the GOP decision, which they viewed as an "anti-free-market" intervention. (Comment: The textile industry is one of Pakistan's most important economic sectors. Skyrocketing cotton prices have caused considerable turmoil in recent weeks, adding misery to an industry that has been significantly affected by rising costs of inputs attributed to the local electricity and gas shortages. The

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GOP's decision to limit yarn exports, which could be challenged under WTO regulations, will reduce Pakistan's foreign exchange earnings, but will help to preserve some desperately needed jobs in central Punjab. End Comment)

ENERGY & WATER

¶6. (SBU) Local political party challenges electricity tariff hike. On January 8, the Daily Times reported that the Lahore High Court (LHC) accepted a petition from the Jamaat-e-Islami (JeI) party challenging the National Electric Power Regulatory Authority's recent decision to increase the electricity tariff by 18 percent, in October and January, claiming that the move was unconstitutional. The LHC scheduled a hearing on this matter for January 21. (Comment: JeI is trying to capitalize on popular discontent with rising electricity costs and persistently dismal service. There is little basis upon which to seriously question the legitimacy of NEPRA's actions. By agreeing to hear the case, the LHC has made clear its intent to meddle in issues related to energy tariffs. This is a worrying sign, as the LHC intervention in a case involving sugar prices earlier this year resulted in massive disruptions of sugar supplies. End Comment)

¶7. (SBU) Lucky Cement signs Memorandum of Understanding (MoU) with Oracle Coal Fields. On January 8, Business Day reported that under this MoU, Sindh Carbon Energy Limited, a subsidiary of Oracle Coal Fields, will mine the coal to be supplied to Lucky Cement's plants. Oracle Coal Fields currently has an exploration license for Block 4 of the Thar Coal Field. (Comment: Contacts at Lucky Cement confirmed the report and expect the project will encourage exploration and mining of the Thar coal field, while helping to both reduce dependence on imported coal and increase Pakistan's foreign exchange reserves. End Comment)

AGRICULTURE

¶8. (SBU) Ministry of Food and Agriculture (MinFA) hoping to sign Memorandum of Understanding (MoU) with Monsanto. The News reported, on January 9, that MinFA is particularly interested in introducing Monsanto's insect-resistant strand of cotton seed into the local

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market. However, while the Ministry of Law and Justice recently cleared on the draft MoU, the Ministries of Textiles, Finance, Commerce, Environment, and Science and Technology and the provincial Ministries of Agriculture have yet to review the document. (Comment: Pakistan is the world's fourth-largest cotton producer, third largest raw cotton exporter and a leading yarn exporter. However, its cotton yield per acre is 13th in the world. The Monsanto agreement would help to increase per acre cotton production. End Comment)

¶9. (SBU) GOP removes taxes on imported sugar. The News reported on January 13 that Finance Minister Shaukat Tarin had confirmed the GOP would scrap the 16 percent sales tax and all other duties on white and refined sugar to facilitate import of the commodity by non-state importers. The move comes as Pakistan faces a growing shortage of white sugar. The GOP is looking to import 1.25 million tons of sugar to help fill this supply gap. (Comment: This artificially created sugar shortage is primarily attributed to the GOP's clumsy intervention in the market, setting local sugar prices significantly lower than international prices thus encouraging rent seeking behavior and hoarding. End Comment)

STOCK MARKET

¶10. (SBU) Karachi Stock Exchange (KSE). The Karachi Stock Exchange (KSE)-100 Index closed on January 18 at 9,895.46, a 0.1 percent increase from the previous week's close. Overall market

capitalization slightly increased to \$33.74 billion, with a net foreign portfolio inflow of \$6.84 million. Stabilizing macroeconomic indicators and the projected 3.3 percent growth in GDP were the major driving forces keeping the market optimistic. (Comment: Our KSE contact said the persistent inflow of foreign portfolio investment and the inflow of funds from the IMF were buoying the market. End Comment)

¶11. (SBU) Lahore Stock Exchange (LSE). According to Business Recorder, banking and oil stocks pushed the LSE Index up 5.76 percent in the first half of January. The LSE index passed 3,000 on January 4 and has stayed above that mark since. Volume and trading were heavier than average, and market capitalization was up 4.5 percent.

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